

Inspector General

United States
Department of Defense



2003 Real Estate Transactions of the Armed Forces
Retirement Home - Gulfport

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Acronyms and Abbreviations

AFRH	Armed Forces Retirement Home
COO	Chief Operating Officer
GSA	General Services Administration
H.R.	House of Representatives
IG	Inspector General
NAVFAC	Naval Facilities Engineering Command
NDAA	National Defense Authorization Act
USD(P&R)	Under Secretary of Defense for Personnel and Readiness



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

February 22, 2010

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE FOR PERSONNEL
AND READINESS
NAVAL INSPECTOR GENERAL
CHIEF OPERATING OFFICER, ARMED FORCES
RETIREMENT HOME

SUBJECT: 2003 Real Estate Transactions of the Armed Forces Retirement Home –
Gulfport (Report No. D-2010-045)

We are providing this report for your information and use. We performed this audit in response to language contained in the report of House Armed Services Committee accompanying H.R. 2647 (H. Rept 111-166), the National Defense Authorization Act for FY 2010. The report required the DOD Office of Inspector General to review the Armed Forces Retirement Home's 2003 real estate transactions in Gulfport, Mississippi. We considered management comments on a draft of this report when preparing the final report.

The comments of the Deputy Under Secretary of Defense (Military Community and Family Policy) conformed to the requirements of DOD Directive 7650.3. Therefore, additional comments are not required.

We appreciate the courtesies extended to the staff. Please direct questions to me at (703) 604-9201 (DSN 664-9201).

A handwritten signature in cursive script, reading "Richard B. Jolliffe", is positioned above the printed name.

Richard B. Jolliffe
Assistant Inspector General
Acquisition and Contract Management



Results in Brief: 2003 Real Estate Transactions of the Armed Forces Retirement Home - Gulfport

What We Did

We initiated the audit in response to language contained in the report of the House Armed Services Committee accompanying H.R. 2647 (H. Rept 111-166), the National Defense Authorization Act for FY 2010. The report required the DOD Office of Inspector General to review the 2003 real estate transactions by the Armed Forces Retirement Home (AFRH) in Gulfport, Mississippi.

We determined whether AFRH complied with applicable laws and regulations when conducting its real estate transactions in Gulfport. We reviewed the decisions that led to the real estate transactions and determined whether AFRH followed appropriate procedures.

What We Found

We identified internal control weaknesses related to AFRH's 2003 real estate transactions in Gulfport. AFRH officials acted within the authority given to them under Public Law 107-107, "National Defense Authorization Act for FY 2002" (FY 2002 NDAA), when acquiring a 10.02-acre parcel of property adjacent to the AFRH-Gulfport facility and subsequently disposing of the two beachfront properties included in the parcel. AFRH was required under the FY 2002 NDAA to acquire the parcel. The FY 2002 NDAA also gave AFRH the authority to dispose of property that it determined to be "excess to the needs of the Retirement Home." As a result, AFRH officials purchased the 10.02-acre parcel for about \$5.7 million and subsequently sold the

two beachfront parcels for about \$1 million. However, if AFRH officials had required appraisals of the two beachfront properties before the sale, officials may have been able to sell the properties for a higher amount, resulting in additional money for the AFRH Trust Fund. In addition, the use of separate real estate agents could have decreased the appearance of a conflict of interest and increased documentation of the negotiations.

What We Recommend

We recommend that the Chief Operating Officer, AFRH, in future disposals of excess property:

- Obtain an appraisal by an accredited appraiser of the property to be disposed of.
- Maintain adequate documentation of the rationale for and process followed in all real estate transactions, including negotiations between AFRH and any potential buyers.

Management Comments and Our Responses

The Deputy Under Secretary of Defense (Military Community and Family Policy) agreed with both recommendations. The Deputy's comments meet the intent of the recommendations. No additional comments are required.

Recommendations Table

Management	Recommendations Requiring Comment	No Additional Comments Required
Chief Operating Officer, Armed Forces Retirement Home		1, 2

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Introduction

Objectives

The overall objective of the audit was to determine whether the Armed Forces Retirement Home (AFRH) complied with applicable laws and regulations when conducting its real estate transactions. We reviewed the decisions that led to the real estate transactions and determined whether AFRH followed appropriate procedures during the acquisition, modification, and sale of the property. We also reviewed other issues related to the real estate transactions. See the Appendix for the scope and methodology related to the objectives.

Background

This audit was initiated in response to language contained in the report of the House Armed Services Committee accompanying H.R. 2647 (H. Rept 111-166), the National Defense Authorization Act for FY 2010. The report required the DOD Office of Inspector General (IG) to review the AFRH 2003 real estate transactions and subsequent boundary adjustments in Gulfport, Mississippi, including:

- (1) The intent or purpose behind AFRH's decision to acquire and subsequently sell the property within such a short period of time;
- (2) If appropriate procedures were followed in the acquisition, modification of parcel boundaries, and sale of the beachfront parcels, including an examination of whether the appraisals, property listings, surveys, and bid offerings followed generally accepted practices; and
- (3) Other issues related to the overall real estate transaction.

Congressman Gene Taylor also raised concerns about the real estate transactions. On February 3, 2009, Congressman Taylor wrote a letter to the Secretary of Defense outlining concerns about the acquisition and subsequent sale of real property of AFRH in Gulfport, specifically regarding the appraisal and sale values of the two beachfront properties.

AFRH

According to the AFRH Web site, the U.S. Soldiers' and Airmen's Home located in Washington, D.C., was merged into a single agency with the U.S. Naval Home in Gulfport in 1991. The U.S. Naval Home originally opened in Philadelphia in 1834; the Gulfport location was developed in the late 1960s when the Philadelphia facility could no longer be modernized and expanded to meet the needs of the home. In 2001, Congress established AFRH as an independent organization in the executive branch and changed the name of the U.S. Soldier's and Airmen's Home to AFRH-Washington and the name of the U.S. Naval Home to AFRH-Gulfport. AFRH is partially funded by withholdings

from active-duty Service members, fines, and interest from the AFRH Trust Fund. The AFRH mission is to fulfill our Nation's commitment to its veterans by providing a premier retirement community.

Before Hurricane Katrina damaged the site in August 2005, AFRH planned to renovate and expand the Gulfport facility. AFRH received authorization to use funds from the AFRH Trust Fund for this renovation and expansion in Public Law 107-107, the FY 2002 NDAA, subject to the review and approval of the Secretary of Defense. Subsequently, extensive damage to the AFRH-Gulfport facility from Hurricane Katrina resulted in the demolition of the facility and plans for the construction of a new facility. The new facility is scheduled to be completed in 2010 and estimated to cost about \$194 million, according to the AFRH-Gulfport Web site.

FY 2002 NDAA

The FY 2002 NDAA established AFRH as an independent entity in the executive branch and designated the Chief Operating Officer (COO) of AFRH as the head of the retirement home, subject to the authority, direction, and control of the Secretary of Defense. The Act required the existing AFRH Board to continue to serve until the Secretary of Defense appointed the first COO, who would then take over the duties of the Board. The Act established the process AFRH uses for purchasing and disposing of property. The Act states:

The Secretary of Defense may acquire, for the benefit of the Retirement Home, property and facilities for inclusion in the Retirement Home. The Secretary of Defense may dispose of any property of the Retirement Home, by sale, lease, or otherwise, that the Secretary determines is excess to the needs of the Retirement Home. The proceeds from such a disposal of property shall be deposited in the Armed Forces Retirement Home Trust Fund. No such disposal of real property shall be effective earlier than 120 days after the date on which the Secretary transmits a notification of the proposed disposal to the Committees on Armed Services of the Senate and the House of Representatives.

The FY 2002 NDAA also allowed AFRH to use money from the AFRH Trust Fund for the expansion of the AFRH-Gulfport facility. The FY 2002 NDAA authorized the use of \$22.4 million from the AFRH Trust Fund, subject to the review and approval of the Secretary of Defense, for the development and construction of a blended-use, multicare facility and for the acquisition of a parcel of real property adjacent to the retirement home consisting of approximately 15 acres.

Office of the Under Secretary of Defense for Personnel and Readiness

The Principal Deputy Under Secretary of Defense for Personnel and Readiness [USD(P&R)] is responsible for the selection, overall supervision, performance evaluation, compensation, and termination of the AFRH COO. The COO reports to the Principal Deputy USD(P&R) through the Deputy Under Secretary of Defense (Military

Community and Family Policy) and the Principal Director in the Office of the Deputy Under Secretary of Defense (Military Community and Family Policy), who have day-to-day oversight of policy and congressional matters regarding AFRH.

Review of Internal Controls

DOD Instruction 5010.40, “Managers’ Internal Control (MIC) Program Procedures,” January 4, 2006, requires DOD organizations to implement a comprehensive system of internal controls that provides reasonable assurance that programs are operating as intended and to evaluate the effectiveness of the controls. We identified internal control weaknesses in the way that AFRH conducted its real estate transactions. AFRH officials did not perform an appraisal before the sale of the two beachfront properties; the buyer used the same real estate agent that AFRH officials listed the beachfront properties with, creating the appearance of a conflict of interest; and AFRH and did not adequately document price negotiations during the sale of the two beachfront properties.

Implementing Recommendations 1 and 2 will improve the process AFRH follows in future AFRH real estate transactions. We will provide a copy of the report to the senior officials responsible for internal controls in the Office of USD(P&R) and AFRH.

Finding. The Armed Forces Retirement Home's Purchase and Subsequent Sale of Property in Gulfport, Mississippi

AFRH officials acted within the authority given to them under the FY 2002 NDAA when acquiring a 10.02-acre parcel of property adjacent to the AFRH-Gulfport facility and subsequently disposing of the two beachfront properties contained in the parcel. The FY 2002 NDAA required AFRH to acquire the parcel. The FY 2002 NDAA also gave AFRH, subject to the review and approval of the Secretary of Defense, the authority to dispose of property determined to be "excess to the needs of the Retirement Home."

- AFRH intended to purchase the 10.02 acres for about \$1 to \$2 million to expand AFRH-Gulfport into a blended-use, multicare facility; however, the purchase price increased to about \$5.7 million, reducing the amount available for construction. To recoup some of the funds, AFRH officials divided the 10.02 acres into three parcels and sold the two beachfront parcels including the homes located on the parcels.
- Appraisal Associates and Ladner Appraisal Group, Inc., each prepared appraisals of the 10.02-acre parcel that conformed to generally accepted practices. City of Gulfport officials followed applicable laws and regulations when approving the AFRH application to modify parcel boundaries of the 10.02 acres. AFRH officials did not have an appraisal done of the two beachfront parcels before the sale and instead had two Gulfport real estate agencies conduct market surveys to determine the listing prices. The buyer used the same real estate agent that AFRH officials listed the beachfront properties with. AFRH officials stated they accepted the offers on the two beachfront properties without documenting price negotiations.
- We did not find any other issues related to the overall real estate transactions.

As a result, AFRH officials purchased the 10.02-acre parcel for about \$5.7 million and subsequently sold the two beachfront parcels for about \$1 million. However, if AFRH officials had required appraisals of the beachfront parcels before the sale, officials may have been able to sell the properties for a higher amount, resulting in additional money for the AFRH Trust Fund. In addition, the use of separate real estate agents could have eliminated the appearance of a conflict of interest and increased documentation of the negotiations.

AFRH Authority to Purchase and Sell Property

AFRH officials acted within the authority given to them under the FY 2002 NDAA during the purchase, resubdivision, and subsequent sale of property adjacent to the AFRH-Gulfport facility. The FY 2002 NDAA required AFRH to purchase the available

10.02-acre parcel¹ adjacent to the AFRH-Gulfport facility. The 10.02 acres contained three parcels: Johnson Tract, located at 1804 Beach Drive (1.44 acres); Eleanor Culler Tract I, located at 1814 Beach Drive (1.01 acres); and Eleanor Culler Tract II, located behind 1804 and 1814 Beach Drive² (7.57 acres). The FY 2002 NDAA authorized AFRH officials to use \$22.4 million out of the AFRH Trust Fund and required that the funds be made available, subject to the review and approval of the Secretary of Defense, for the “development and construction of a blended use, multicare facility at the Naval Home”³ and “for the acquisition of a parcel of real property adjacent to the Naval Home consisting of approximately 15 acres.” AFRH purchased the property for about \$5.7 million, which it withdrew from the AFRH Trust Fund. As a result of AFRH officials purchasing the property at a significantly higher price than anticipated, AFRH incurred additional costs and liabilities that reduced the funds available for the construction of the blended-use, multicare facility. According to AFRH officials, to recoup some of the funds, they divided the 10.02 acres into three parcels and sold the two beachfront parcels and the homes located on the parcels. AFRH officials stated the sale resulted in about \$1 million in proceeds, which AFRH officials deposited into the AFRH Trust Fund. Figure 1 shows an aerial view of the AFRH-Gulfport facility. The area outlined in red is the 10.02-acre parcel originally purchased by AFRH. The dashed white lines indicate the beachfront parcels that were subsequently sold by AFRH. The structure circled in yellow is the only part of the new AFRH-Gulfport facility that is positioned on the 10.02-acre parcel.

¹ The FY 2002 NDAA listed the parcel as 15 acres for estimation purposes only. The true size of the parcel of land AFRH intended to purchase was 10.02 acres.

² The street addresses of the two beachfront properties are referred to in some documents as East Beach Drive or Beach Boulevard.

³The FY 2002 NDAA changed the name of the Naval Home to the Armed Forces Retirement Home.

Figure 1. Aerial View of the AFRH-Gulfport Facility



Note: All the markings on Figure 1 are approximate and were added by the audit team.

Source: AFRH

FY 2010 NDAA Issues and DOD IG Responses

DOD IG was required by the House of Representatives version of the FY 2010 NDAA to review AFRH's 2003 real estate transactions and subsequent boundary adjustments in Gulfport. Specifically, H.R. 2647 required DOD IG to review:

- (1) The intent or purpose behind AFRH's decision to acquire and subsequently sell the property within such a short period of time;
- (2) If appropriate procedures were followed in the acquisition, modification of parcel boundaries, and sale of the beachfront parcels, including an examination of whether the appraisals, property listings, surveys, and bid offerings followed generally accepted practices; and
- (3) Other issues related to the overall real estate transaction.

Public Law 111-84, the FY 2010 NDAA, did not include the above language. However, because of congressional concern over the real estate transactions, we discuss the issues identified in H.R. 2647 in the sections that follow.

Issue 1

"The intent or purpose behind AFRH's decision to acquire and subsequently sell the property within such a short period of time."

DOD IG Response

AFRH intended to purchase the 10.02 acres for about \$1 to \$2 million to expand the AFRH-Gulfport facility; however, the purchase price increased to about \$5.7 million, reducing the amount available for construction of the blended-use, multicare facility. AFRH officials stated that, to recoup some of the funds, they divided the 10.02 acres into three parcels and sold the two beachfront parcels, including the homes located on the parcels, to increase the AFRH Trust Fund balance.

Increased Sale Price of the 10.02 Acres

The AFRH Board anticipated purchasing the 10.02 acres for about \$1.4 million; however, the Naval Facilities Engineering Command (NAVFAC) had a second appraisal and a land survey completed on the property, resulting in an increased assemblage value of about \$5.2 million. Appraisal Associates performed the first appraisal of the three parcels of land. Appraisal Associates valued the 1804 Beach Drive parcel at \$450,000; the 1814 Beach Drive parcel at \$475,000; and the back parcel at \$473,000. The date of the appraisals was March 20, 2001. Appraisal Associates did not provide an appraised value on the assemblage of the three parcels, but provided the appraised value of about \$1.4 million by combining the three parcels' appraised values. AFRH officials authorized NAVFAC officials to begin negotiations for the acquisition of the three parcels on October 29, 2001, and NAVFAC officials completed a review of the Appraisal Associates appraisals on December 20, 2001. The NAVFAC reviewer stated that the fair market value estimates in the appraisals were subjective and lacked sufficient support for the reviewer to concur with the value estimates. The reviewer recommended that NAVFAC contract with another independent appraiser to provide the values required for negotiations for the acquisition of the property.

At the request of NAVFAC officials, Ladner Appraisal Group, Inc., performed another appraisal, which significantly increased the appraised value of the properties. Ladner Appraisal Group, Inc., valued the 1804 Beach Drive parcel at \$860,000; the 1814 Beach Drive parcel at \$750,000; and the back parcel at \$950,000. Ladner Appraisal Group, Inc., also valued the assemblage of the three parcels at \$5.1 million on February 21, 2002.

NAVFAC officials reviewed the Ladner Appraisal Group, Inc., appraisal on April 12, 2002, and found that the appraised acreages varied from the surveyed acreages. Cassady & Associates, Inc., completed the final land survey of the properties after the appraisal, and the acreage for 1804 Beach Drive and the back parcel were slightly different. The 1804 Beach Drive property lost 0.03 acres, which did not affect the appraised value, while the back parcel gained 0.29 acres. The reviewer and the appraiser discussed and reconciled the final appraised values based on the changes. The appraiser concluded that the additional land would change the back parcel's value to \$990,000 and the revised value for the combined parcels—that is, the assemblage value—to about \$5.2 million. Table 1 shows the appraised values determined by Appraisal Associates and Ladner Appraisal Group, Inc., and the recommended NAVFAC values.

Table 1. Appraised Values and NAVFAC Recommendations

Tract	Appraisal Associates' March 20, 2001, Appraisal¹	Ladner Appraisal Group, Inc.'s February 21, 2002, Appraisal¹	NAVFAC Recommendation April 12, 2002²
1804 Beach Drive (Johnson Tract)	\$450,000	\$860,000	\$860,000
1814 Beach Drive (Eleanor Culler Tract I)	\$475,000	\$750,000	\$750,000
Back Parcel (Eleanor Culler Tract II)	\$473,000	\$950,000	\$990,000
Assemblage Value	Not Applicable	\$5,100,000	\$5,235,000

¹Dates listed are the value dates of the land appraisals.

²NAVFAC officials also considered the Cassidy & Associates, Inc., survey results when determining the recommended assemblage value.

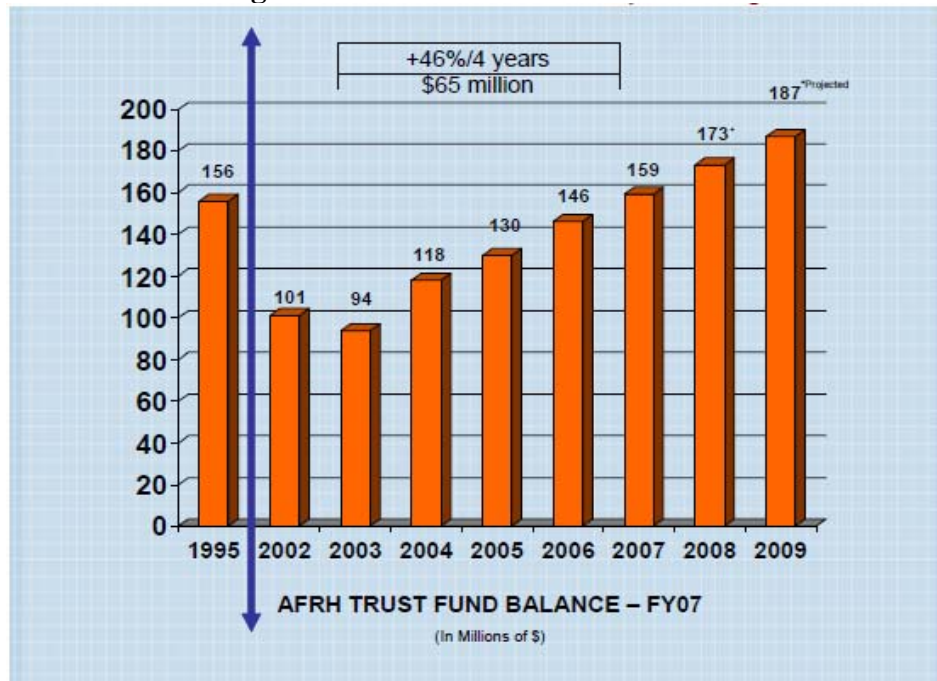
NAVFAC officials began negotiating the purchase agreement for AFRH by offering \$5.1 million on March 13, 2002. Previously, the owners had asked about \$6.1 million for the property. NAVFAC officials and the owners negotiated a purchase price of about \$5.6 million for the 10.02-acre parcel on March 19, 2002. After the adjustment in appraised values because of the final surveyed acreages, NAVFAC officials negotiated with the owners and adjusted the purchase price for the property to about \$5.7 million.

AFRH Trust Fund Balance

The AFRH COO stated AFRH officials purchased the 10.02-acre parcel with money from the AFRH Trust Fund, which had a declining balance. The purchase put further financial strain on the AFRH Trust Fund. The Office of Management and Budget expressed concerns about AFRH's financial solvency. Figure 2 shows the AFRH Trust Fund Balance in 2002,⁴ the year of the acquisition.

⁴ We did not validate the AFRH Trust Fund balance.

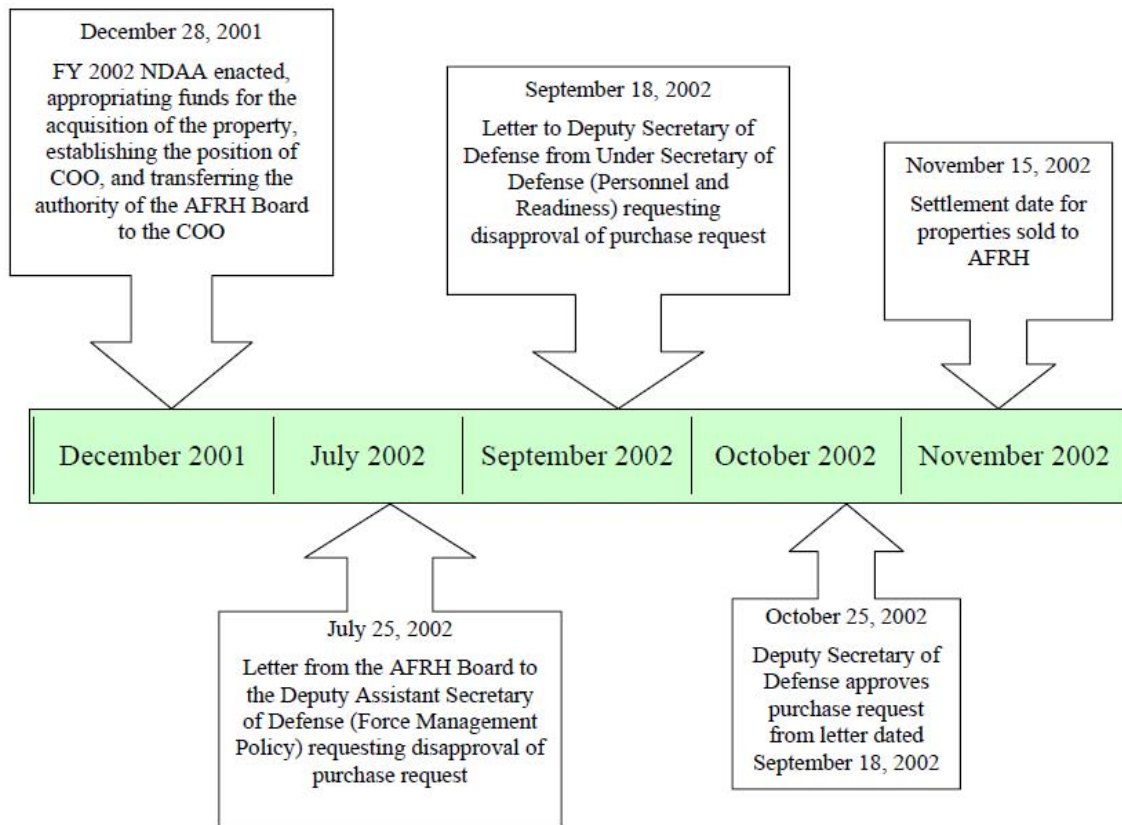
Figure 2. AFRH Trust Fund Balance



Source: AFRH Congressional Justification FY 2009

According to AFRH officials, because of the Trust Fund's declining financial position, AFRH had already cut personnel and other costs. In light of this, the AFRH Board believed that the purchase price was too high and inquired about purchasing only the back parcel at a price consistent with the appraisal for the single parcel. However, the property owners were only willing to sell the three parcels as one parcel. In a letter to the Deputy Secretary of Defense recommending disapproval of the purchase request, the USD(P&R) stated that the AFRH Trust Fund would not be able to support the debt that would be necessary for the construction of the multicare facility if required to purchase the land. However, the Deputy Secretary of Defense approved the purchase request on October 25, 2002. The final settlement date for the purchase was November 15, 2002. Figure 3 shows the timeline for the acquisition of the property.

Figure 3. Timeline of Acquisition of Property



Construction Fund

AFRH officials purchased the 10.02 acres using part of the \$22.4 million designated for expansion of the property and new construction as required by the FY 2002 NDAA. The purchase created a shortfall of funds necessary to complete the construction of the blended-use, multicare facility. The AFRH Board's preliminary plans for the blended-use, multicare facility estimated the costs of construction to be from \$25 million to \$27 million. The FY 2002 NDAA authorized only \$22.4 million, subject to the review and approval of the Secretary of Defense, of which a portion was required to be used to purchase the adjacent property. AFRH officials purchased the property for about \$5.7 million of the \$22.4 million available, leaving AFRH officials with a shortfall of approximately \$10 to \$12 million. AFRH officials would need to finance this shortfall to complete the construction, further straining the AFRH Trust Fund. According to the USD(P&R), the AFRH Trust Fund could not support the debt required to make up the difference. The Chairman of the AFRH Board stated that the acquisition of the land at about \$5.7 million would "seriously compromise an appropriate level of funding needed for construction of the blended use, multicare facility at Gulfport." The AFRH Board viewed the construction of a blended-use, multicare facility as a higher priority than the purchase of land for future uses.

Beachfront Properties

AFRH officials decided to sell the two beachfront properties, located at 1804 and 1814 Beach Drive, to prevent further maintenance liability, to increase the AFRH Trust Fund balance, and because AFRH needed only the back portion of the parcel for the expansion of the retirement home. The two excess parcels included two homes that would have required extensive repairs to be useful to the retirement home. Both homes needed extensive upgrades on the power, water, heating, and air-conditioning systems, as well as many interior renovations. The AFRH COO stated one home had been vacant for more than a year, and mold was present on the walls and surfaces. Because of the distance from the retirement home, AFRH officials would also need to install separate security lighting if AFRH officials decided to keep the homes. In response to questions from the Deputy Under Secretary of Defense (Military Community and Family Policy), the AFRH COO stated, “AFRH has no extra funds to warrant maintaining these homes for future use because they are unneeded in our master plan.” According to AFRH officials, AFRH would have incurred additional costs if AFRH officials had decided to keep the two beachfront homes. Figures 4 and 5 show some of the damage to 1804 and 1814 Beach Drive.

Figures 4 and 5. Damage to Beachfront Homes



Source: USD(P&R)

In addition to the added cost and liability, AFRH officials did not need the property to immediately support the AFRH mission. In a letter from the AFRH Board to the Deputy Under Secretary of Defense (Military Community and Family Policy) requesting that the purchase request be disapproved, the Chairman of the Board stated that the AFRH Executive Committee concluded “while the additional land has potential long-term strategic value, it is not clear that the land is needed to make campus improvements to serve the actuarially projected population of AFRH-Gulfport through at least 2020.” The AFRH COO stated that as a result of the sale of the beachfront properties, \$933,806.20 was deposited into the AFRH Trust Fund.

Issue 2

“If appropriate procedures were followed in the acquisition, modification of parcel boundaries and sale of the beachfront parcels, including an examination of whether the appraisals, property listings, surveys, and bid offerings followed generally accepted practices.”

DOD IG Response

Appraisal Associates and Ladner Appraisal Group, Inc., each prepared appraisals on the property that conformed to generally accepted practices. City of Gulfport officials followed applicable laws and regulations when approving the AFRH application to modify parcel boundaries of the 10.02 acres. AFRH officials acted within the authority given to them in the FY 2002 NDAA when disposing of the two beachfront properties. AFRH officials did not have an appraisal done of the two beachfront parcels before the sale but instead had market surveys completed. The buyer used the same real estate agent that AFRH officials listed the beachfront properties with. In addition, according to AFRH officials, they accepted the offers on the two beachfront properties without documenting negotiations for a higher price.

Appraisal Associates’ Appraisals for the 10.02 Acres

According to NAVFAC officials, Appraisal Associates performed appraisals of the three tracts contained in the 10.02-acre parcel that complied with the Uniform Standards of Professional Appraisal Practice. NAVFAC officials completed a review of the Appraisal Associates appraisals on December 20, 2001, and found that the appraisal reports met Uniform Standards of Professional Appraisal Practice reporting requirements. However, the NAVFAC reviewer stated that the fair market value estimates were subjective and lacked sufficient support for the reviewer to concur with the value estimates. The reviewer recommended that NAVFAC contract with another independent appraiser to provide the values required for negotiations for the acquisition of the property.

Ladner Appraisal Group, Inc., Appraisal for the 10.02 Acres

NAVFAC officials stated Ladner Appraisal Group, Inc., performed a second appraisal on the 10.02-acre parcel that used an appraisal methodology consistent with generally accepted appraisal principles and provided the basis for a credible analysis. NAVFAC officials reviewed the appraisal for compliance with Uniform Standards of Professional Appraisal Practice and the Uniform Appraisal Standards for Federal Land Acquisition.

Resubdivision of the 10.02 Acres

AFRH officials stated after they acquired the 10.02-acre parcel, they resubdivided the 10.02 acres to sell the beachfront properties and replenish the AFRH Trust Fund. Originally, the 10.02-acre parcel adjacent to the AFRH-Gulfport facility was divided into three separate parcels: Johnson Tract, located at 1804 Beach Drive (1.44 acres); Eleanor Culler Tract I, located at 1814 Beach Drive (1.01 acres); and Eleanor Culler Tract II, located behind 1804 and 1814 Beach Drive (7.57 acres). AFRH officials purchased these three parcels totaling 10.02 acres although, according to the AFRH COO, AFRH needed

only about 5 acres of the back portion of the 10.02 acres. Therefore, AFRH officials divided the land into three parcels and sold the two beachfront parcels. The AFRH COO stated that a fence behind the homes was used to determine the property lines, leaving AFRH with about 6 acres. AFRH officials applied to the City of Gulfport for the resubdivision of the 10.02 acres on January 30, 2003. City of Gulfport officials approved the AFRH application on May 15, 2003. Table 2 shows the original parcel sizes before AFRH purchased the 10.02 acres, and the resubdivided parcel sizes according to USD(P&R).

Table 2. 10.02-Acre Resubdivision

Parcel	Original Size (acres)	Size After Resubdivision (acres)
1804 Beach Drive	1.44	1.42
1814 Beach Drive	1.01	2.39
Eleanor Culler Tract II (retained by AFRH)	7.57	6.21
Total	10.02	10.02

Source: USD(P&R)

Sale of Beachfront Properties

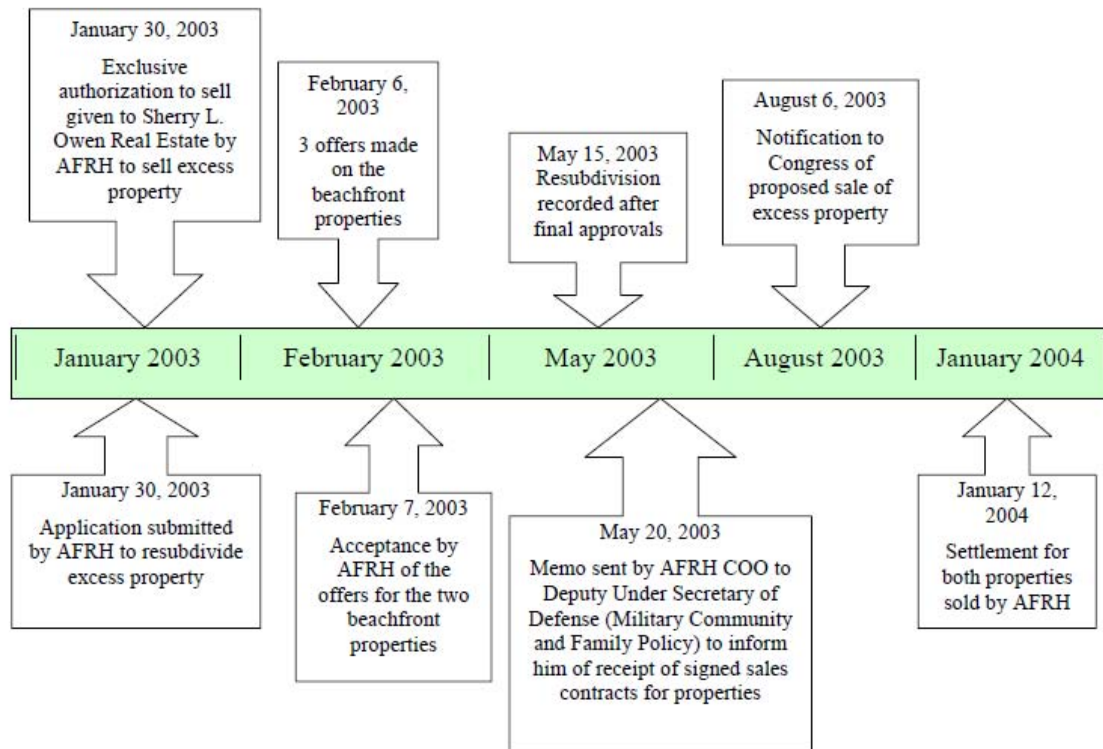
AFRH officials acted within the authority given to them under the FY 2002 NDAA when disposing of the two beachfront properties. The FY 2002 NDAA established the process AFRH officials can use for purchasing and disposing of property. For disposing of property the Act states:

The Secretary of Defense may dispose of any property of the Retirement Home, by sale, lease, or otherwise, that the Secretary determines is excess to the needs of the Retirement Home. . . No such disposal of real property shall be effective earlier than 120 days after the date on which the Secretary transmits a notification of the proposed disposal to the Committees on Armed Services of the Senate and the House of Representatives.

On May 20, 2003, the AFRH COO sent a memorandum to the Deputy Under Secretary of Defense (Military Community and Family Policy) informing him of the receipt of two signed sales contracts for 1804 and 1814 Beach Drive. In the memorandum, the AFRH COO stated that the beachfront land had never been utilized by the Federal Government in any capacity and requested that notification letters be forwarded to the House and Senate Armed Services Committees. On August 6, 2003, the Principal Deputy of the Office of the USD(P&R) sent letters to the Chairmen of the House and Senate Armed Services Committees informing them of the proposed disposal of real property of the AFRH. In the letter, the Principal Deputy stated that he decided to accept the offers on 1804 and 1814 Beach Drive, pending notification of the Senate and House Armed Services Committees, 120 days before the completion of the sale. On January 12, 2004,

159 days after the notification to the Senate and House Armed Services Committees, the sale of the properties was finalized. Figure 6 shows the timeline of the sale of the properties.

Figure 6. Timeline of Disposal of Beachfront Properties



In accordance with the FY 2002 NDAA, AFRH officials stated about \$934,000 was deposited into the AFRH Trust Fund from the sale of the properties. The FY 2002 NDAA stated that, “The proceeds from such a disposal of property shall be deposited in the Armed Forces Retirement Home Trust Fund.” AFRH officials deposited a total of \$933,806.20 into the AFRH Trust Fund after settlement charges were paid. Of the \$933,806.20, \$421,766.60 were proceeds from the sale of 1804 Beach Drive, and \$512,039.60 were proceeds from the sale of 1814 Beach Drive. Table 3 shows the expenses and amounts paid by AFRH and by the buyers.

Table 3. Expenses Paid by AFRH and Buyers, by Property

Item	Property			
	1804 Beach Drive		1814 Beach Drive	
Sale Price	\$450,000		\$550,000	
Expenses	Paid by AFRH	Paid by Buyer	Paid by AFRH	Paid by Buyer
Commission	\$27,000.00		\$33,000.00	
Loan fees and lender charges	\$24.50	\$4,996.34	\$3,361.50	\$6,426.05
Title, recording, and transferring charges	\$725.00	\$1,057.50	\$825.00	\$1,110.00
Additional charges	\$483.90		\$773.90	
Total Expenses	<u>(\$28,233.40)</u>	\$6,053.84	<u>(\$37,960.40)</u>	\$7,536.05
Total deposited into AFRH Trust Fund	\$421,766.60		\$512,039.60	

Appraisals of Beachfront Parcels

According to the AFRH COO, AFRH officials did not have appraisals completed of the two beachfront properties before the sale. The AFRH COO stated that two Gulfport real estate agencies conducted market surveys of comparable sales in the area to determine an acceptable listing price. The real estate agencies compared the two beachfront properties with beachfront homes sold within the past 18 months. The real estate agent stated the seller (AFRH COO) decided on the listing prices, and on January 30, 2003, the AFRH COO listed 1804 Beach Drive for \$542,000 and 1814 Beach Drive for \$687,762.

However, AFRH should have had an appraisal conducted of the two beachfront properties by an accredited appraiser before the sale to ensure the listing prices were consistent with the fair market value of the properties and to avoid the appearance of any impropriety. Table 4 shows the listing prices compared with the earlier appraised values.

Table 4. Listing Price Compared With Appraised Values

Property	Appraisal Associates' March 20, 2001, Appraisals¹	Ladner Appraisal Group, Inc.'s February 21, 2002, Appraisal¹	Listing Price² January 30, 2003
1804 Beach Drive	\$450,000 ³	\$860,000 ³	\$542,000
1814 Beach Drive	\$475,000 ⁴	\$750,000 ⁴	\$687,762

¹Dates listed are the value dates of the land appraisals.

²The market surveys determined the listing prices, not the appraisals.

³Appraised values were determined when 1804 Beach Drive was .048 acres larger than when the listing price was determined.

⁴Appraised values were determined when 1814 Beach Drive was 1.38 acres smaller than when the listing price was determined.

General Services Administration Procedures

AFRH officials stated they did not use the General Services Administration (GSA) to dispose of the beachfront properties. Generally, Federal agencies go through GSA to dispose of excess real property. However, annotated section 411, title 24, United States Code, "Hospitals and Asylums," states that "the Secretary of Defense may dispose of any property of the Retirement Home, by sale, lease, or otherwise, that the Secretary determines is excess to the needs of the Retirement Home." The proceeds will then be deposited into the AFRH Trust Fund. The GSA Federal Management Regulation, 41 CFR parts 102-71 and 102-72 (November 8, 2005), states that GSA encourages agencies with independent disposal authority to take advantage of services from agencies with expertise in real property disposal. AFRH officials chose to sell the property through a local real estate agency rather than go through GSA. The GSA Federal Management Regulation also states that appraisals are generally required for all property disposal transactions except when an appraisal will serve no useful purpose or when the property does not exceed \$300,000. AFRH officials sold both properties for more than \$300,000 each. The market surveys completed by the realtor were reflected in the respective listing prices of \$542,000 for 1804 Beach Drive and \$687,762 for 1814 Beach Drive.

AFRH officials may have sold the property for the same value or less if they had used GSA to dispose of the two beachfront properties. The GSA Federal Management Regulation outlines the standard procedures for the acquisition, management, utilization, and disposal of real property. Specifically, if a Federal agency finds it has excess real property, agency officials will determine whether there is any other Federal need for the property. After the agency determines there is no longer a Federal need, the property is made available for acquisition by State and local governments. If State and local government officials do not have a need for the property, it will be made available to nonprofit organizations or sold to the public through advertising, negotiation, or other disposal action. GSA Real Estate Division officials confirmed that this is the standard

procedure followed for the disposal of excess property. GSA officials offered to handle the disposal of the AFRH property by selling the beachfront parcels. The GSA offer to sell the beachfront parcels included marketing efforts such as preparing briefing booklets to present to the House and Senate Armed Services Committees, listing the properties on the GSA Web site, placing ads in local newspapers, and preparing the closing documents. According to the AFRH COO's letter to the Deputy Under Secretary of Defense (Military Community and Family Policy), the COO asked GSA officials how they would dispose of the property; they said they would have auctioned the two properties and estimated that the AFRH would have received about \$400,000 per home. The AFRH COO stated that he decided against using GSA to sell the property because he concluded that doing so would result in a lower sale value than listing the properties with a real estate agent. As a result, AFRH officials may not have realized a higher sales price for the two beachfront properties by using GSA; in fact, the sale may have resulted in a smaller or no deposit into the AFRH Trust Fund.

Use of Dual Real Estate Agent

The buyer used the same real estate agent that AFRH officials listed the property with, an arrangement that could create the appearance of a conflict of interest. Both the AFRH COO and the real estate agent confirmed that AFRH officials and the buyer used the same realtor to negotiate and complete the sale of the beachfront properties. The AFRH COO stated he contacted the office of a Member of Congress for the name of a real estate agent specializing in Gulf coast properties to use to sell the properties. According to the AFRH COO, after AFRH officials had listed the beachfront properties with the agent, the buyer decided to use the same real estate agent to avoid paying additional commission fees. The AFRH COO and the buyer signed a dual-agency confirmation, giving their consent to use the same realtor to complete the real estate transaction. The dual-agency confirmation explained that a disclosed dual agent is a licensee who, with the informed written consent of the seller and buyer, is engaged as the agent for both the seller and the buyer. The dual-agency confirmation also explained that the disclosed dual agent does not represent the interests of one party to the exclusion of the interests of the other party. The AFRH COO stated that he and the buyer conducted all negotiations verbally through the real estate agent and did not document the negotiations that determined the final purchase price. Using a separate real estate agent could have decreased the appearance of a conflict of interest and also could have increased documentation of the negotiations.

Negotiation Documentation

The AFRH officials generally followed appropriate procedures during the sale of the two beachfront parcels. However, the AFRH officials stated they accepted the offers on the two beachfront properties without documenting negotiations. On February 6, 2003, two different buyers submitted a total of three offers on the two beachfront parcels. One buyer submitted an offer for 1814 Beach Drive with a purchase price of \$600,000. The real estate agent stated that the buyer's offer was an either/or offer, which included another purchase price of \$700,000 if additional land was included with 1814 Beach Drive. The other buyer submitted two offers: an offer for 1804 Beach Drive with a purchase price of \$450,000 and a second offer for 1814 Beach Drive with a purchase price of \$550,000. The AFRH COO accepted the two offers from the buyer who

submitted offers for both 1804 and 1814 Beach Drive. According to the AFRH COO, he accepted these offers because they enabled him to dispose of both beachfront parcels. The AFRH COO stated he negotiated the sale price verbally through the real estate agent, using as a benchmark for the negotiations the market survey completed before the properties were listed. The AFRH COO also stated that all negotiations were verbal, and once he and the buyer agreed on a price, the offer was submitted and accepted. The real estate agent stated a majority of her real estate files and documentation were destroyed during Hurricane Katrina. The AFRH COO and the real estate agent should have documented the negotiations. Figure 7 shows the beachfront parcels, 1804 and 1814 Beach Drive, as photographed in September 2009.

Figure 7. 1804 and 1814 Beach Drive



Issue 3

“Other issues related to the overall real estate transaction.”

DOD IG Response

We did not identify any other issues related to the overall real estate transactions.

Conclusion

AFRH officials acted within the authority given to them under the FY 2002 NDAA when acquiring a 10.02-acre parcel of property adjacent to the AFRH-Gulfport facility and subsequently disposing of the two beachfront properties. Under the FY 2002 NDAA, AFRH officials were required to use \$22.4 million from the AFRH Trust Fund for the construction of the AFRH-Gulfport facility and for the acquisition of a parcel of real property adjacent to the home. AFRH officials intended to purchase the 10.02 acres for about \$1.4 million to expand the AFRH-Gulfport facility; however, the purchase price increased to about \$5.7 million, reducing the amount available for construction of the

blended-use, multicare facility, AFRH officials divided the 10.02 acres into three parcels and sold the two beachfront parcels including homes located on the parcels. As a result of the sale, AFRH deposited \$933,806.20 into the AFRH Trust Fund. Appraisal Associates and Ladner Appraisal Group, Inc., each prepared appraisals that conformed to accepted practices before AFRH purchased the parcel. City of Gulfport officials followed applicable laws and regulations for approving the AFRH application to modify parcel boundaries of the 10.02 acres. However, AFRH did not have an appraisal done of the two beachfront parcels before the sale according to the AFRH COO; the buyer used the same real estate agent that AFRH officials listed the properties with; and AFRH accepted the offers on the two beachfront properties without documenting price negotiations. We believe the process for conducting real estate transactions could have been improved had AFRH officials had an appraisal completed of the two beachfront properties before selling them and maintained adequate documentation of the rationale for and process followed in all real estate transactions.

Recommendations, Management Comments, and Our Response

We recommend that the Chief Operating Officer, Armed Forces Retirement Home, in future disposals of excess property:

- 1. Obtain an appraisal by an accredited appraiser of the property to be disposed of.**

Management Comments

The Deputy Under Secretary of Defense (Military Community and Family Policy) agreed and stated that AFRH will follow the requirements of Public Law 111-288, the FY 2010 NDAA, in future disposals of excess property. The Deputy Under Secretary also noted that the market comparisons AFRH relied on for this transaction provided a selling price that was within the range of the two government-sponsored appraisals.

Our Response

The comments were responsive, and no additional comments are required. Public Law 111-288, the FY 2010 NDAA, requires the Secretary of Defense to be authorized by law prior to acquiring real property costing more than \$750,000 for inclusion in the Retirement Home. If the Secretary of Defense determines that any property of the Retirement Home is excess, the Secretary must dispose of the property in accordance with subchapter III, title 40, chapter 5, United State Code, "Public Buildings, Property, and Works."

- 2. Maintain adequate documentation of the rationale for and process followed in all real estate transactions, including negotiations between the Armed Forces Retirement Home and any potential buyers.**

Management Comments

The Deputy Under Secretary of Defense (Military Community and Family Policy) agreed and stated that AFRH has followed guidance including Public Law 107- 107; the NDAA for Fiscal Year 2002; OMB Circular A-124 [*sic*; A-123], “Management’s Responsibility for Internal Controls,” December 21, 2004; Government Accountability Office Report No. GAO-01-1008G, “Internal Control Management and Evaluation Tool,” August 2001; the Federal Managers’ Financial Integrity Act; section 3512, title 31 United States Code; and predecessor guidance of the information currently contained in the AFRH’s Internal Control Notice.

Our Response

The comments were responsive, and no additional comments are required.

Appendix. Scope and Methodology

We conducted this performance audit from July 2009 through January 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

We did not validate the AFRH Trust Fund balance; however, the balance may have been validated by another organization. We were unable to ensure that we obtained all documentation on the sale of the beachfront properties as a result of files lost in the wake of Hurricane Katrina.

This audit was initiated in response to language contained in the report of the House Armed Services Committee accompanying H.R. 2647 (H. Rept 111-166), the National Defense Authorization Act for FY 2010. The report required DOD IG to review the AFRH's 2003 real estate transactions and subsequent boundary adjustments in Gulfport.

Congressman Gene Taylor also raised concerns about real estate transactions. Congressman Taylor wrote a letter to the Secretary of Defense on February 3, 2009, outlining concerns about the acquisition and subsequent sale of real property of the AFRH in Gulfport, Mississippi. Concerns expressed in this letter included appraisal and sale values of the beachfront properties.

We obtained and reviewed the Federal Property and Administrative Services Act of 1949; Public Law 107-107, "National Defense Authorization Act for FY 2002"; Public Law 107-314, "National Defense Authorization Act for FY 2003"; Public Law 108-136, "National Defense Authorization Act for FY 2004"; annotated section 411, title 24, United States Code, "Hospitals and Asylums"; the GSA Federal Management Regulation, 41 CFR sections 102-71 and 102-72; subchapter III, title 42, chapter 61, United States Code, "Uniform Real Property Acquisition Policy"; and City of Gulfport Ordinance 2608.

We also obtained and reviewed Gulfport real estate listings; appraisal of the property completed by Ladner Appraisal Group, Inc., dated March 11, 2002; appraisals of the property completed by Appraisal Associates dated April 3, 2001; NAVFAC reviews of the appraisals dated December 20, 2001, and April 12, 2002; the scope of work for the appraisal dated January 24, 2002; the invitation to bid on properties dated January 24, 2002; AFRH Board minutes; settlement statements dated November 15, 2002, and January 12, 2004; and a warranty deed dated November 26, 2002. In addition, we reviewed the contract for appraisal services between NAVFAC and Ladner Appraisal Group, Inc., contract N62467-02-RP-00074, dated February 15, 2002.

We interviewed staff from the AFRH in Washington, D.C., and Gulfport; USD (P&R) officials in Washington, D.C.; NAVFAC officials in Washington, D.C., and Jacksonville, Florida; and GSA officials in Washington, D.C., to determine their understanding and involvement in the 2003 AFRH real estate transactions.

We interviewed the real estate agent in Gulfport who handled the sale of the AFRH property to obtain information on standard real estate procedures and the processes the real estate agent followed during the sale.

We interviewed City of Gulfport zoning officials to obtain information regarding the resubdivision of land before AFRH sold the property. We reviewed property records at the Harrison County Chancery Clerk's office in Gulfport, Mississippi.

Use of Computer-Processed Data

We did not use computer-processed data to perform this audit.

Prior Coverage

No audits have been conducted on the real estate transactions of the AFRH – Gulfport during the last 5 years.

Deputy Under Secretary of Defense (Military Community and Family Policy) Comments



PERSONNEL AND
READINESS

OFFICE OF THE UNDER SECRETARY OF DEFENSE
4000 DEFENSE PENTAGON
WASHINGTON, D.C. 20301-4000

JAN 20 2010

Inspector General
Department of Defense
[REDACTED]
400 Army Navy Drive
Arlington, VA 22202-4704

Dear [REDACTED]

Thank you for the opportunity to comment on this very professional, thorough, and well researched audit report of the 2003 Real Estate Transactions of the Armed Forces Retirement Home (AFRH) – Gulfport. AFRH response to the recommendations is as follows:

- **Recommendation: Obtain an appraisal by an accredited appraiser of the property to be disposed of.**
 - **AFRH Response:** Concur. In future disposals of excess property, AFRH will comply with new requirements contained in the Public Law 111-288, the National Defense Authorization Act for FY10. Of note, in this instance relying on market comparisons, which is customary in real estate transactions, provided AFRH with a realistic selling price that was within the range of the two government sponsored appraisals.
- **Recommendation: Maintain adequate documentation of the rationale for and process followed in all real estate transactions, including negotiations between AFRH and any potential buyers.**
 - **AFRH Response:** Concur.

The Department is pleased the report concludes that AFRH officials acted within the authority given under Public Law 107-107, NDAA for Fiscal Year 2002 when acquiring a 10.02 acre parcel of property adjacent to AFRH-Gulfport and subsequently disposing of the two beachfront properties included in the parcel. Historically, the AFRH has followed the intent and spirit of current pertinent Administration guidance such as OMB Circular A-124, Management's Responsibility for Internal Controls the GAO Internal Control Management and Evaluation Tool, the Federal Managers' Financial Integrity Act (FMFIA) 31 USC 3512 and predecessor

guidance of the information currently contained in the AFRH's Internal Control Notice.

Thank you for your continued support of our nation's veterans.

Sincerely,

A handwritten signature in black ink, appearing to read "Tommy T. Thomas". The signature is fluid and cursive, with a large initial "T" and a stylized "H".

Tommy T. Thomas
Deputy Under Secretary of Defense
(Military Community and Family Policy)

Copy to:
AFRH COO



Inspector General Department of Defense

